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SUBJECT: CASPIAN PIPELINE CONSORTIUM: STATE OF PLAY  
KAZAKHSTAN

Classified By: CLASSIFIED BY CDA MARK ASQUINO FOR REASONS 1.4 (B) AND (D)

1. (C) Summary: The April 26th Caspian Pipeline Consortium (CPC) shareholders meeting in Almaty ended in an impasse. Russian intransigence on forming a Russian board of directors (CPC-R), combined with a demand for a variable tariff on operating expenses (OPEX), created the logjam. In earlier meetings with Ambassador Ordway, ChevronTexaco Eurasian Business Chief Guy Hollingsworth and ExxonMobil Kazakhstan Country Representative David Willis were vexed over Moscow's hard-line. Both were united in opposition to a CPC-R board of directors. The companies split, however, over an OPEX variable tariff, with ExxonMobil bitterly opposed and ChevronTexaco flexible. Corporate shareholders will not, barring some Russian concession, attend a May 16th meeting with Russian Energy Minister Khristenko. End Summary.

No Movement at CPC Shareholders Meeting

2. (C) Guests at an April 26th gala dinner for CPC shareholders were, in the words of one participant, &down in the mouth.8 Shell Kazakhstan Country Manager Martin Ferstl, host of the event, told DCM Mark Asquino that the shareholders came out of the meeting &at sword points8 because the Russians &had taken a hard-line.8

3. (C) The Russians pushed hard on creating a board of directors for CPC-R and gaining a variable tariff for both CAPEX and OPEX. Oleg Gordiyev, Deputy Director of Energy, complained that CPC was in debt \$5bn and needed to recoup this loss. He added that the oil companies &did not understand this.8 When queried as to a middle ground between Russia and other consortium members, Gordiyev fell silent.

4. (C) ChevronTexaco Eurasia Business Chief Guy Hollingsworth vowed that his company &would not give into the charter (with board of directors).8 Some of the other oilies posited that if the consortium could not come to terms on a charter for CPC-R, Nazarbayev and Putin would have to personally engage. Ferstl of Shell, however, doubted the extent to which Nazarbayev could push Putin.

5. (C) According to Ferstl, Western CPC shareholders unofficially decided not to attend a May 16th meeting with Russian Energy Minister Khristenko barring some Russian concession. GOK Energy Minister Vladimir Shkolnik announced the May 16th Moscow talks in Astana on May 4.

ExxonMobil: &At the Walk-Away Point8

6. (C) ExxonMobil Kazakhstan Country Chairman David Willis told Ambassador Ordway in an April 15th meeting that ExxonMobil was at its &walk-away point8 on CPC expansion. He added that, &We have offered about all that we can give.8 Willis said ExxonMobil was amenable to an immediate tariff increase as well as to a variable tariff to capture CAPEX cost overruns, but was adamantly opposed to a variable tariff on OPEX. It would, according to him, create a further divide between shippers and non-shippers and be liable to machinations.

7. (C) Russia,s drive to create a board of directors for CPC-R, however, is the ultimate redline for ExxonMobil. Willis noted that under the Russian joint stock law, the composition of a board of directors could be changed by a 51% vote. Given that Russia, Kazakhstan, and Oman control 50% already, they, according to Willis, would just need to bribe one minor shareholder to surpass 51%. They then could create a docile board of directors and seize control of CPC. Willis dubbed CPC expansion a &small issue8 compared with the threat a board of directors poses.

8. (C) Willis also sought a new GOR presidential decree confirming the non-natural monopoly status of an expanded CPC. A Yeltsin-era decree affords such protection to the existing pipeline.

ChevronTexaco: Situation Not Yet Critical

9. (C) Guy Hollingsworth, ChevronTexaco Eurasia Business Chief, was more upbeat over CPC expansion than his ExxonMobil partner. In an April 22nd lunch with Ambassador Ordway,

Hollingsworth joked that the Russians would &close at the last minute8. He added that as long as CPC received project sanction by the end of 2005, the situation was ? critical.8

10. (C) While opposed to a board of directors for CPC-R, Hollingsworth was resigned to a variable tariff on OPEX. He said that ChevronTexaco &could go for it8 because it would not be &catastrophic8 and would add only about \$1-2 per barrel cost (Note: When it comes on line in mid-2006, TengizChevroil,s (TCO) &Second Generation8 project will add about 250,000 bpd of production. TCO, operated with a 50% stake by ChevronTexaco, will scramble to find export routes for the added crude until CPC expansion becomes operational. At minimum, there will be an 18 month lag. End Note).

11. (C) Hollingsworth hinted that President Nazarbayev, who calls CPC &my pipeline8, would intervene against Russia. &The President likes us. We perform.8 (Comment: ChevronTexaco prides itself on its &special relationship8 with the Kazakhstanis given its status as the first major Western investor. This relationship extends to presidential son-in-law and hydrocarbon Richelieu, Timur Kulibayev. End Comment)

12. (C) Comment: Real issues separate CPC private sector shareholders. None unites them as much, however, as their opposition to a Russian-controlled puppet board of directors. If Russia wants to kill expansion, that demand will be more than a mere bargaining chip for a variable tariff on OPEX. The three-year\*and counting\*CPC expansion process should serve as wake-up call for both the GOK and private producers to get serious on other pipeline options. Three million barrel a day production is not far off\*most experts point to 2015. It could ramp up to four to five million barrels a day by 2020-25 given the right tax regime. According to Hollingsworth, Kazakhstan will need four additional pipelines to bring that amount of oil to world markets.  
ASQUINO

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